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SUBJECT: 2010 GOVERNMENT OF IRAQ BUDGET

¶1. (SBU) Summary: The Council of Representatives (CoR) passed a Federal Public Budget Law for Fiscal Year 2010 (2010 Budget Law) that made significant amendments to the draft budget law submitted to the CoR by the Council of Ministers (CoM) in October 2009. The 2010 Budget Law increased the stated budget to $72.4 billion, approximately $1.1 billion over the October 2009 draft budget. However, the final 2010 Budget Law also introduced new revenue streams for provincial governments that will increase federal government outlays by several billion dollars, but were not factored into the final budget figures. Provincial governments also received the authority to request the transfer to their control of capital investment projects from several ministries. Further complicating the 2010 Budget Law is a provision freezing the hiring of 115,000 new civil servants. Despite some unanswered questions about the 2010 Budget Law, we expect the staffs of the IMF and the World Bank to recommend that their boards approve the Stand-By Arrangement and the Development Policy Loans. End Summary.

84.7 Trillion Dinar Federal Budget

¶2. (U) On January 26, 2010, the CoR passed a 2010 Budget Law authorizing expenditures of 84.7 trillion IQD, equaling approximately $72.4 billion. This figure is $1.1 billion higher than the $71.3 billion total in the draft budget submitted to the CoR in October 2009. $52.1 billion would be for operating expenditures and $20.3 billion for capital expenditures, with capital expenditures increasing 60 percent over the figure in the 2009 budget.

¶3. (U) Based on oil exports of 2.1 mbpd at an average price of $62.50/barrel, the budget assumes oil revenue of $47.9 billion and non-oil revenue of $4.9 billion, for total revenues of $52.8 billion. The planned deficit would be $19.6 billion. [Note: An average oil price of $70/barrel would result in oil revenue of $53.6 billion, reducing the expected deficit to $13.9 billion. As of January 26, 2010, the export price of Basrah Light crude oil to the U.S. was $69.31/barrel. End note.]

Dollars for the Provinces

¶4. (SBU) The 2010 Budget Law creates new revenue streams for certain provinces, denominated in dollars rather than in Iraqi dinars like all other expenditures in the 2010 Budget Law. Article 43 of the 2010 Budget Law states that, on a monthly basis, the Ministry of Finance (MoF) will add the following amounts for hydrocarbon production or oil refining to the budgets of the relevant provinces:

-- $1 for each barrel of crude oil produced in a province;

-- $1 for each barrel of crude oil refined in a province; and

-- $1 for each 150 cubic meters of natural gas produced in a province.

The same article states that the MoF will allocate $20 from each

entry visa for a foreign visitor to a holy site to the relevant province to be spent for development of the cities of the holy sites. All provinces appear to be eligible for these transfers, not only provinces not associated with the Kurdish Regional Government (KRG). [Note: In 2009 Iraq produced approximately 874 million barrels of crude oil and 64 billion cubic meters of natural gas, refined approximately 103 million barrels of crude oil, and was visited by approximately 6.5 million foreign tourists. The same figures in 2010 would result in $1.5 billion in transfers from the federal government to the provinces. End note.]

¶5. (SBU) Article 42 of the 2010 Budget Law adds a further revenue stream based on customs revenues. This article requires the
Qstream based on customs revenues. This article requires the
Ministry of Finance to allocate 5 percent of customs revenues from each land, air, or sea port of entry to the province of the port of entry. [Note: The 2010 Budget Law estimates customs revenues of approximately $434 million; 5 percent of that amount will be approximately $22 million. End note.]

¶6. (U) These revenue streams are separate from, and in addition to, the regular provincial government budget allocations that are included in the nominal $72.4 billion budget authorization. The 2010 Budget Law allocates approximately $9.1 billion for the KRG and $3.5 billion for provincial governments outside the KRG. There are no provisions for reconciling the newly added revenue streams with the existing provincial budget allocations, other than a requirement that provincial governments amend their budgets and present them to the MoF for approval.

KRG Crude Oil Penalties

¶7. (SBU) The KRG continues to receive a 17 percent share of total expenditures, but with the possibility of penalties for withholding crude oil from the federal government. Article 16 continues the 17 percent share for the KRG, with exclusions for sovereign expenditures that include fees for transportation of crude oil through Turkey. Article 17 has a provision declaring that a resolution should be initiated to determine the damages caused by misappropriation of crude oil by any entity - a declaration aimed primarily at the KRG. Since further legislation will be required for damages to be imposed on the KRG, this provision of the 2010 Budget Law will most likely not be put into effect until after the seating of the new CoR.

Devolution to the Provinces - You Must Whip It
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¶8. (U) The 2010 Budget Law appears to devolve several federal government ministry responsibilities to provincial governments. The provincial governments are expected to assume the social safety net obligations of the Ministry of Labor and Social Affairs, and as a result the $3.5 billion allocation for provincial governments outside the KRG is approximately $1 billion higher than in 2009. Moreover, Sections 3 through 5 of Article 23 direct the Ministry of Finance to transfer the allocations for capital investment projects of the Ministries of Electricity, Municipalities and Public Works, Health, Education, and Housing and Construction to provinces outside of the KRG, at the request of a province and the approval of the provincial council. The provincial councils will supervise the implementation of transferred projects, and the provinces will implement new investment projects. Article 23 also requires provincial councils to submit reports on June 1 regarding transfer requests and any reluctance by ministries to comply. [Note: Under the 2010 Budget Law, the ministries affected by Article 23 have capital investment budgets totaling $7.0 billion (Electricity: $3.5 billion, Municipalities and Public Works: $1.3 billion, Health: $963 million, Education: $427 million, Housing and Construction: $598 million), or $4.6 billion if the $2.4 billion allocated for repayment of 2009 General Electric and Siemens t-bills under the Ministry of Electricity budget is excluded. End note.]

¶9. (U) Article 23 of the 2010 Budget Law accelerates an existing

trend toward decentralization of ministerial budgets and powers to the provinces. The CoR earlier passed a law to abolish the Ministry of Municipalities and Public Works and transfer its functions and budget to the provincial governments. In the draft and final 2010 Budget Law, Article 16 included a provision that commits ministries to distribute their operating and capital investment budgets to the provincial governments outside of the KRG, based on their percentages of Iraq's population. The CoR added Sections 3 through 5 of Article 23 to the final 2010 Budget Law to expand the decentralization process, by going beyond a general commitment to decentralize and creating an opportunity for provincial governments to mandate the transfer of investment projects and budgets.

Hiring of 115,000 Civil Servants Frozen

¶10. (SBU) The 2010 Budget Law authorizes approximately 148,000 more government employees than the 2009 budget law. However, a provision added to Article 21 prohibits hiring 115,000 authorized civil servants until the formation of a Federal Service Council. This organization does not currently exist, and creating it would require
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a law enacted by the CoR. Since the CoR has gone into recess prior to the upcoming election, this provision in effect would freeze hiring of 115,000 civil servants. [Note: The CoM has issued an executive order establishing a Civil Service Joint Coordinating Committee that will perform the role of the Federal Service Council until the latter is created. It is not yet certain whether this committee will be considered a sufficient substitute prior to the formation of a Federal Service Council. End note.]

¶11. (SBU) The 2010 Budget Law does not specify which civil servant positions cannot be filled or how to identify them. Discussions with GOI officials, however, indicate that they include multiple groups, some to be newly hired and others currently paid by the GOI as temporary employees rather than as full-fledged civil servants. The latter includes substantial numbers of transitioned Sons of Iraq members and provincial government employees. These groups will probably remain on the government payroll without an upgrade to civil servant status until the creation of the Federal Service Council. [Note: Sources in IFCNR and the CoR have stated that funding for continued temporary employment of the transitioned Sons of Iraq is secure. End note.]

¶12. (SBU) Prime Minister Maliki's State of Law coalition has voiced its opposition to the restriction on civil service hiring and has called for a veto of the 2010 Budget Law by the Presidency Council. Maliki's political opponents contend that the restriction is necessary to prevent him from hiring new employees as a means to strengthen his position in the upcoming national elections. We deem a veto unlikely.

Comment

¶13. (SBU) As adopted, the budget law creates complicated political issues for the GOI. Enactment of a 2010 GOI budget was the final condition for the IMF and World Bank to consider approval of the IMF Stand-By Arrangement (SBA) and World Bank Development Policy Loans (DPLs). World Bank staff in Baghdad has indicated that despite the $1.1 billion increase in the budget figures and the further undetermined increase caused by the new federal government transfers to provincial governments, World Bank and IMF staff will recommend approval of the SBA and DPLs to their respective boards. However, the call for penalties for misuse of crude oil and the restriction on hiring 115,000 civil servants until creation of a Federal Service Council will be issues for the next CoR after the election. Furthermore, the federalism issues created by the new revenues and powers given to the provinces will need to be addressed in 2010 and possibly beyond. These complications are a consequence of making decisions with significant political implications, and constitutional implications as well, in a budget law.

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